

11 U.S.C. § 503(b)(1)(A)
O.R.S. 441.277 et seq.
Administrative claim

In re Allen Care Centers, Inc., Civil No. 94-726-RE

9/22/94

J. Redden aff'd PSH

The district court affirmed Judge Higdon by sustaining the trustee's objection to the State of Oregon's administrative claim for the cost of closing debtor's nursing home pursuant to state laws designed to safeguard residents' welfare. The state argued that its position was similar to environmental cleanup cases where bankruptcy courts have allowed administrative expense status for expenses incurred in preventing imminent and identifiable harm to public health or safety.

The district court rejected this analogy based on the facts of the case. First, there was no actual benefit to the debtor's estate. A potential tort claim against the estate was not a sufficient benefit. Second, there was no imminent threat to public health and welfare. There was no evidence that the debtor had not provided appropriate care. Third, unlike the environmental cases, this case did not involve a violation of state law.

11 U.S.C. § 503(b)(1)(A)
ORS 441.277 et seq.,
Administrative claim

In re Allen Care Centers, Inc., Civil No. 94-726-RE

9/22/94

J. Redden aff'd PSH

*Published
175 BR 397*

The district court sustained the trustee's objection to the State of Oregon's administrative claim for the cost of closing debtor's nursing home pursuant to state laws designed to safeguard residents' welfare. The state argued that its position was similar to environmental cleanup cases where bankruptcy courts have allowed administrative expense status for expenses incurred in preventing imminent and identifiable harm to public health or safety.

The district court rejected this analogy based on the facts of the case. First, there was no actual benefit to the debtor's estate. A potential tort claim against the estate was not a sufficient benefit. Second, there was no imminent threat to public health and welfare. There was no evidence that the debtor had not provided appropriate care. Third, unlike the environmental cases, this case did not involve a violation of state law.

94 SEP 27 13:48

94 SEP 22 PM 12:03

FILED
CLERK OF DISTRICT COURT
PORTLAND, OREGON

U.S. BANKRUPTCY COURT
DISTRICT OF OREGON
FILED

SEP 22 1994 *lod 9-28-94*

TERENCE H. DUNN, CLERK

BY *W* DEPUTY

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

In re:

ALLEN CARE CENTERS, INC.,
an Oregon corporation,

Debtor.

Civil No. 94-726-RE

Bankr. No. 390-36679-P7

OPINION

Theodore R. Kulongoski
Attorney General of Oregon
Virginia L. Linder
Solicitor General
Stephanie L. Striffler
Assistant Attorney General
400 Justice Building
Salem, Oregon 97310

Attorneys for Appellant State of Oregon

Gregg D. Johnson
Ater Wynne Hewitt Dodson & Skerritt
222 S.W. Columbia, Suite 1800
Portland, Oregon 97201-6618

Attorney for Appellee Ronald G. Witcosky, Trustee

REDDEN, Judge:

The State of Oregon, Department of Human Resources,
Senior & Disabled Services Division (the State), appeals the
order of Bankruptcy Judge Polly Higdon. Under that ruling, the

1 - OPINION

Certified to be a true and correct
copy of original filed in my office.

Dated 9/23/94

Donald M. Cinnamond, Clerk

By *Clara Priestly* Deputy

1 State holds a general, unsecured claim and is not entitled to
2 administrative expense priority under 11 U.S.C. § 503(b)(1)(A)
3 for costs incurred in closing the debtor's nursing facility.
4 Oral argument on appeal was held on September 19, 1994. For
5 the reasons that follow, the order of the bankruptcy court is
6 affirmed.

7 BACKGROUND

8 The debtor, Allen Care Centers, operated three nursing
9 and residential care facilities licensed by the State. Facing
10 financial difficulties, the debtor filed a petition for
11 reorganization under Chapter 11 on December 10, 1990. The case
12 was later converted into a liquidation proceeding under
13 Chapter 7.

14 On December 19, 1990, the debtor contacted the State to
15 discuss closing one of the facilities, Care West. The debtor
16 was concerned that soon it would not be able to meet its
17 operating expenses and wanted the State to seek a trustee to
18 operate and close Care West.

19 Under Oregon law, the State may, under certain
20 circumstances, petition in state court for the appointment of a
21 trustee to operate a nursing facility. See Or. Rev. Stat.
22 441.286 (1993). The trustee's expenses are paid from a state
23 fund and the operator of the facility--the debtor in this
24 case--is responsible for repaying the expenditures. Id.
25 441.303, 441.318(2).

26 \ \ \

1 The debtor filed motions in state and bankruptcy courts
2 aimed at forcing the State to seek appointment of a trustee.
3 In one of the motions, the debtor stated that it was "unable to
4 adequately fund operations, creating threatened staffing
5 problems with the potential to cause physical or mental harm to
6 patients." Excerpt of Record (ER), 261. The State was
7 concerned that the debtor would not be able to reimburse the
8 State fund for expenses the State would incur in closing the
9 facility. ER 294-317.

10 On January 30, 1991, Bankruptcy Judge Elizabeth Perris
11 held a hearing on debtor's motion to abandon Care West. The
12 transcript of the hearing (as well as the preceding state court
13 hearing) reveals that the State delayed seeking a trustee to
14 operate the facility with the hope of obtaining an assurance
15 from the bankruptcy court that the State would receive an
16 administrative expense priority. ER 139-144, 294-317. Judge
17 Perris described the State's actions as "jockeying over
18 economics" and expressed her desire that "the State . . . get
19 on with getting the trustee appointed so that the facility --
20 so that the residents can be placed and the facility can be
21 closed." ER 139-40.

22 Judge Perris refused to give the State any assurance that
23 the trustee's expenses would be treated as administrative
24 expenses (and therefore would be more likely to be recouped)
25 and indicated that the decision would be made only after the
26 expenses were incurred. ER 136-37. Judge Perris's order

3 - OPINION

1 allowed the debtor to "abandon" Care West unless the State
2 obtained a trustee on or before February 1, 1991, in which case
3 the abandonment would occur when the residents of Care West
4 were moved or 60 days from the appointment of the trustee,
5 whichever happened first. ER 159-60.

6 On January 31, 1991, a trustee was appointed and all the
7 residents were moved to other facilities by April 1, 1991. In
8 operating Care West, the trustee incurred expenses of
9 \$232,695.50. Appellee, the bankruptcy trustee, did not object
10 to payment of \$102,695.50 of the expenses because they were
11 incurred by debtor before the State took over the facility.

12 In a written memorandum opinion, Judge Higdon rejected
13 the State's claim that the costs it incurred were
14 administrative expenses under § 503(b). Memorandum Opinion,
15 January 19, 1994.

16 STANDARDS FOR REVIEW

17 The bankruptcy court's conclusions of law are reviewed de
18 novo by this court. In re Kennerley, 995 F.2d 145, 146 (9th
19 Cir. 1993). The bankruptcy court's findings of fact are
20 reviewed under the "clearly erroneous" standard. Fed. R.
21 Bankr. P. 8013; Kennerley, 995 F.2d at 146.

22 DISCUSSION

23 A bankruptcy judge has "broad discretion in determining
24 whether to award administrative expense priority." In re Dant
25 & Russell, Inc., 853 F.2d 700, 706 (9th Cir. 1988).

26 Administrative expenses are "the actual, necessary costs and

1 expense of preserving the estate[.]" 11 U.S.C. § 503(b).

2 The State argues that its trustee's expenses in operating
3 Care West and transferring elderly residents to other
4 facilities fit this definition. It relies on analogies to the
5 progeny of two Supreme Court cases, Midlantic National Bank v.
6 New Jersey Dept. of Envir. Protection, 474 U.S. 494 (1986), and
7 Reading Co. v. Brown, 391 U.S. 471 (1968).

8 1. Midlantic

9 In Midlantic, the Court held that a debtor could not
10 "abandon" estate property in contravention of state and federal
11 laws designed to protect public health and safety. Midlantic,
12 474 U.S. at 507. The Court emphasized that the exception
13 created by its holding was narrow. Id. at n.9. Since then,
14 courts have held that if environmentally contaminated property
15 cannot be abandoned in violation of the law, then expenses
16 incurred by others to clean-up environmental contamination of
17 the debtor's estate are administrative expenses. See, e.g., In
18 re Peerless Painting, 70 B.R. 943 (W.D. Mich. 1987), In re
19 Stevens, 68 B.R. 774, 783 (D. Me. 1987).

20 By analogy, the State argues that the debtor could not
21 have "abandoned" Care West without complying with state law
22 ensuring the health and safety of the residents. Therefore,
23 the State's expenditures, like expenditures to clean-up
24 environmental contamination, are administrative expenses.

25 The Ninth Circuit construes administrative expenses
26 narrowly. "Any claim for administrative expenses and costs

1 must be the actual and necessary costs of preserving the estate
2 for the benefit of its creditors." Dant & Russell, 853 F.2d at
3 706. In Dant & Russell, the court emphasized that the benefit
4 to the estate must be "actual" and not potential. Id. These
5 principles were recently emphasized by the bankruptcy appellate
6 panel for the Ninth Circuit. In re Daniel C. Hanna, 168 B.R.
7 386, 388 (Bankr. 9th Cir. 1994).

8 The State's analogy to the environmental cases fails when
9 the facts of this case are analyzed. First, in this case there
10 was no actual benefit to the debtor's estate. While it is
11 unquestionable that the residents of Care West benefitted from
12 the State's action, under Dant & Russell, there must be actual
13 benefit to the debtor's estate. See In re Woodstock Associates
14 I, 120 B.R. 436, 452 (N.D. Ill. 1990) (holding that nursing
15 home operating expenses did not benefit the estate).

16 The State argues that if it had not stepped in the
17 residents, deprived of proper care, would have brought tort
18 claims against the estate, depleting its assets. This
19 potential benefit does not suffice. Dant & Russell, 853 F.2d
20 at 706 ("the mere potential of benefit to the estate does not
21 satisfy this requirement"). The Ninth Circuit in Dant &
22 Russell distinguished between environmental cases where the
23 estate owned, rather than leased, the contaminated realty. Id.
24 at 709. In the former, the estate benefitted from clean-up
25 expenditures. In the latter, it did not. Id. In both cases,
26 the estate faces potential tort liability from the effects of

1 the contamination. Therefore, averting potential tort claims,
2 alone, does not benefit the estate.

3 Second, contrary to the State's contention, there was no
4 imminent threat to public health and welfare. The record
5 reveals that the State delayed seeking a trustee to operate the
6 debtor's facility because it was concerned about protecting its
7 financial position. In fact, the bankruptcy court prodded the
8 State to seek the trustee. This "jockeying over economics," as
9 Judge Perris described it, suggests that the threat to the
10 patients' health was not imminent. As the bankruptcy court
11 properly found, there was "no evidence . . . that at any time
12 up to the appointment of the state trustee the debtor or debtor
13 in possession had not provided appropriate care." Memorandum
14 Opinion, 6. Thus, the harm faced was not imminent and is not
15 analogous to the threats from hazardous wastes in the
16 environmental cases relied upon by the State.

17 Third, this case, unlike the environmental cases, does
18 not involve a violation of law by the debtor. While the
19 debtor, in a motion filed in January 1991, stated that it was
20 "unable to adequately fund operations, creating threatened
21 staffing problems with the potential to cause physical or
22 mental harm to patients," the record does not establish that
23 the debtor violated any law protecting the health and safety of
24 its patients. Judge Higdon's finding, that the debtor did not
25 violate state or federal law protecting health and safety, was
26 not clearly erroneous.

7 - OPINION

1 In short, Judge Higdon was correct in finding that the
2 environmental clean-up expense cases following Midlantic are
3 not analogous to the facts of this case and that the Ninth
4 Circuit's reasoning in Dant & Russell supports denial of
5 administrative expense priority where the estate has received
6 no benefit.

7 2. Reading

8 In Reading, the Supreme Court held that payments to
9 victims of the bankruptcy trustee's negligence were
10 administrative expenses. Reading, 391 U.S. at 485. Lower
11 courts have followed Reading and given administrative expense
12 priority to expenses paid for the torts of the debtor or
13 trustee. See, e.g., In re Charlesbank Laundry, 755 F.2d 200
14 (1st Cir. 1985) (expenses incurred from civil penalties from
15 violation of an injunction by the trustee), In re N.P. Mining
16 Co., 963 F.2d 1449 (11th Cir. 1992) (penalties for
17 environmental violations), In re Vermont Real Estate Inv.
18 Trust, 25 B.R. 804 (Bankr. D. Vt. 1982) (expenses to abate
19 nuisance).

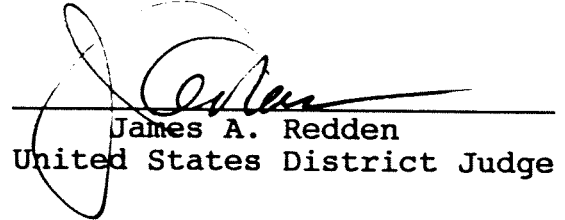
20 However, as Judge Higdon noted, there is no evidence of
21 debtor negligence or wrongdoing that would bring this case
22 within the narrow rule of Reading.

23 CONCLUSION

24 Although it is unfortunate that the State is left with an
25 unsecured claim for its expenses, here Judge Higdon, in a well-
26 reasoned opinion, reached the correct result. The bankruptcy

1 court's order is, therefore, affirmed.

2 Dated this 22 day of September, 1994.

3
4
5 
6 James A. Redden
7 United States District Judge
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26